

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF DELAWARE

In re:	)	Chapter 7
	)	Case No. 01-1430 (JBR)
WINSTAR COMMUNICATIONS, INC., <i>et al.</i> ,	)	
	)	Jointly Administered
Debtors.	)	
	)	

**MEMORANDUM OPINION**

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Dated: November 14, 2003

**ROSENTHAL, J.**

**FACTS**

Before the Court is BEA Systems, Inc.'s ("BEA") Motion For Relief From Stay and to Allow Exercise of Setoff Rights (Doc. # 3878) and the Trustee's<sup>1</sup> Demand for Turnover of Estate Property Pursuant to 11 U.S.C. §§ 105, 541, 542 and 543 (Doc. # 3937). After briefing by the parties and oral argument, and for the reasons set forth below, BEA's Motion is DENIED and the Trustee's Demand for Turnover of Estate Property is GRANTED.

Since the parties agreed that no factual dispute exists (no evidentiary hearing was requested or held), the Court briefly states the facts as follows. Prepetition, Winstar Communications, Inc. (the "Debtors" or "Winstar") and BEA entered into a three-year Software License Agreement to provide Winstar with certain software, support and maintenance services.

On or about November 5, 1999 (the "November 1999 Sale"), BEA sold software, and provided support and maintenance for the software to Winstar in the amount of \$8,575,000. In connection with the sale, Winstar paid sales taxes in the amount of \$350,437.50 to BEA as agent for the Commonwealth of Virginia. See Va. Code Ann. § 58.1-625. Subsequent to Winstar's filing for bankruptcy protection, Winstar advised BEA of Winstar's tax exemption<sup>2</sup> and BEA filed an amended tax return with the State of Virginia seeking a refund of the sales tax paid in connection with the November 1999 Sale. The State of Virginia refunded BEA the sales tax and accrued interest for a total of \$437,963.26.

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<sup>1</sup> Christine C. Shubert, the chapter 7 trustee in the Winstar Communications, Inc. bankruptcy cases.

<sup>2</sup> It is unnecessary to decide whether Winstar requested BEA to file the tax return.

The Debtors filed for protection under Chapter 11 of the Bankruptcy Code on April 18, 2001. The Debtors' Chapter 11 was converted to a liquidation case under Chapter 7 of the Bankruptcy Code in January of 2002. BEA filed a proof of claim for its prepetition unsecured claim in the amount of \$1,740,037.50 for unpaid software and services.

### **DISCUSSION**

The Bankruptcy Code does not create the right to set off but provides for the exercise of a right to setoff by giving the creditor, who has a right to setoff, a secured status. See In re Delta Energy Resources, 67 B.R. 8, 10 (Bankr.W.D.La. 1986). Section 553 provides in pertinent part:

Except as otherwise provided in this section and in sections 362 and 363 of this title, this title does not affect any right of a creditor to offset a mutual debt owing by such creditor to the debtor that arose before the commencement of the case under this title against a claim of such creditor against the debtor that arose before the commencement of the case...

11 U.S.C. § 553.

In order for a creditor to establish its rights under § 553, the creditor must show the following:

- 1) a debt owed by the creditor to the debtor which arose prior to the commencement of the bankruptcy case;
- 2) a claim of the creditor against the debtor which arose prior to the commencement of the bankruptcy case; and
- 3) the debt and claim must be mutual obligations.

Michigan Consol. Gas Co. v. Fred Sanders Co. (In re Fred Sanders), 33 B.R. 310, 311 (Bankr.E.D.Mich. 1983), quoting, Waldschmidt v. Columbia Gulf Transmission Co. (In re Fulghum Construction Corp.), 23 B.R. 147, 151 (Bankr.M.D.Tenn. 1982). Moreover, for the debt and the claim to be a mutual obligation it "must be in the same right and

between the same parties, standing in the same capacity.” Id. at 312, quoting, Collier on Bankruptcy ¶ 553 at 553-22 (15<sup>th</sup> ed. 1983).

Here, there is no mutuality of obligations. BEA has a claim against the Debtors for software and services rendered from October 30, 2000 through October 29, 2001, and consulting services rendered from October 2000 through March 2001. However, the tax refund claim is from the November 1999 Sale. More specifically, BEA collected and remitted the taxes from the November 1999 Sale in its capacity as agent for the Commonwealth of Virginia. The Virginia Statute on tax collocation provides in part that “[a]ll sums collected by a dealer... shall be deemed to be held in trust for the Commonwealth.” Va. Code Ann. §58.1-625. Having realized that Winstar was exempt from paying taxes on the November 1999 Sale, Winstar advised BEA of the exemption and BEA filed an amended tax return with the Commonwealth of Virginia. Thereafter, the State of Virginia refunded the sales tax with interest in the amount of \$437,963.26 to BEA. Thus, BEA received the refund in an agency capacity and not individually. Because BEA received and holds the tax refund as agent for the Commonwealth of Virginia, BEA is directed to turnover the refund in the amount of \$437,963.26, plus all interest accrued thereon that BEA is presently holding, as it constitutes property of the Debtors’ estates.

Having determined that no mutuality exists, the Court will not address the issues as to whether the tax refund is a prepetition or a postpetition claim.

Moreover, the Court is not making a determination that BEA’s failure to assert its right to setoff on in its proof of claim constitutes a waiver of its right to setoff, since at the time the proof of claim was filed BEA was unaware they had a setoff claim.

## **CONCLUSION**

For the foregoing reasons, the Court denies BEA's Motion for Relief From Stay and to Allow Exercise of Setoff Rights, and grants Winstar's request for an Order Compelling Turnover of Estate Property Pursuant to 11 U.S.C. §§ 105, 541, 542 and 543.

A separate order will be issued.

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Joel B. Rosenthal  
United States Bankruptcy Judge

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF DELAWARE**

In re:	:	CHAPTER 7
WINSTAR COMMUNICATIONS, INC., <i>et al.</i> ,	:	CASE NO. 01-1430 (LK)
Debtors.	:	(Jointly Administered)
	:	<b>RELATED DOCKET #</b>
	:	<b>Hearing Date: to be determined</b>
	:	<b>Objection Deadline: September 5, 2003</b>
	:	<b>Reply Deadline: September 12, 2003</b>

**ORDER (i) DENYING MOTION OF BEA SYSTEMS, INC. FOR RELIEF  
FROM STAY TO EFFECT SETOFF AND (ii) COMPELLING TURNOVER  
OF ESTATE PROPERTY PURSUANT TO 11 U.S.C. §§ 105, 541 AND 542**

Upon the Objection<sup>1</sup> of the Trustee and request for an order (i) denying BEA's motion and (ii) compelling BEA to turnover \$437,963.26 in property of the Debtors' estates, as more fully set forth in the Objection; the Court having read and considered BEA's motion, the Trustee's Objection, further responsive pleadings by the parties, if any, and a hearing regarding this matter having been held; and the Court having jurisdiction to consider the Objection and the relief requested therein in accordance with 28 U.S.C. §§ 157 and 1334; and after due deliberation and sufficient cause appearing therefor; it is hereby

**ORDERED THAT:**

1. BEA's motion is denied in all respects.
2. The Refund in the amount of \$437,963.26, plus all interest accrued thereon, that BEA is presently holding on behalf of the Trustee constitutes property of the Debtors' estates.
3. BEA is required to immediately turnover to the Trustee \$437,963.26 plus interest.

<sup>1</sup> Capitalized terms not otherwise defined herein shall have the meanings ascribed to them in the accompanying Objection.

4. This Court shall retain exclusive jurisdiction to construe and enforce the terms of this Order and to grant such other relief as appropriate.

11/14/03

  
UNITED STATES BANKRUPTCY JUDGE